

4.6 AUDITOR GENERALS REPORT

REPORT OF THE AUDITOR-GENERAL TO THE NORTH WEST PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF THE MAFIKENG LOCAL MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2009

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the accompanying financial statements of the Mafikeng Local Municipality which comprise the balance sheet as at 30 June 2009, and the income statement, and the cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages 85 to 105.

The accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the entity-specific basis of accounting as set out in accounting policy note 1.1 and in the manner required by the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

The Auditor-General's responsibility

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the International Standards on Auditing and General Notice 616 of 2008, issued in Government Gazette No. 31057 of 15 May 2008. Because of the matters described in the Basis for disclaimer of opinion paragraphs, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer of opinion

Cash and bank

4. I was unable to obtain sufficient appropriate audit evidence for journals amounting to R14 800 544 posted against the bank account. Furthermore an unexplained difference of R2 425 033 existed between cash and bank as disclosed in the balance sheet and the year end bank reconciliation. The completeness, existence, rights and obligations, and valuation could not be confirmed or verified.

Investments

5. I was unable to obtain sufficient appropriate audit evidence for journals amounting to R5 553 234 posted against investments. Furthermore, bank confirmations were not received for all investments accounts held by the municipality. Therefore, the completeness, valuation, existence, and rights and obligations of investments to the amount of R20 640 894 could not be verified. No alternative procedures could be performed.



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Property, plant and equipment

6. I was unable to confirm or verify the completeness, valuation and existence of fixed assets to the value of R117 620 000, included in the balance sheet. Land assets belonging to the municipality amounting to R335 690 716 was not included in the fixed asset register or the financial statements. As a result both fixed assets and appropriations were understated by R335 690 716. Furthermore, an unexplained difference of R5 829 552 existed between the asset register and the financial statements.
7. The source of funding for assets amounting to R273 597 799 could not be traced to the loans redeemed and other capital receipts. Therefore I was unable to confirm or verify by alternative means the valuation of loans redeemed and other receipts amounting to R273 597 799.
8. An unexplained difference of R17 876 665 existed between the opening balance of fixed assets, as disclosed in note 6 in the financial statement, and the balance sheet amount of R325 548 155.
9. I was unable to obtain sufficient appropriate audit evidence for infrastructure additions amounting to R6 432 000. The existence, rights and obligations, and valuation of these purchases could not be confirmed.

Long-term liabilities

10. I was unable to obtain sufficient appropriate audit evidence for journals amounting to R22 669 961 posted against long-term liabilities. The valuation, existence, and rights and obligations of these long-term liabilities could not be confirmed.
11. I was unable to confirm the completeness, existence and valuation of the securities held over loans amounting R7 266 919, which was not disclosed in note 4 to the financial statements.

Receivables

12. The bad debt provision included consumer debtors of R232 189 400 and is understated by R43 588 657 in note 10 to the financial statements. Had this amount been included in the provision for bad debts, consumer debtors would have been stated as R188 600 743 since bad debt provision increased by R43 588 657.
13. I was unable to confirm the valuation and existence of debtors to the amount of R11 122 584. These debtors did not make any payments after year-end and alternative attempts to verify these balances were unsuccessful.
14. A difference of R17 246 989 exists between the amount disclosed in the financial statements as consumer debtors and the ageing amount. Had this amount been correctly disclosed, consumer debtors would have been stated as R264 548 792 while creditors would have increased by an amount of R15 112 403 and appropriations by an amount of R2 134 585.
15. I was unable to obtain sufficient, appropriate audit evidence for sundry debtors and debtors in credit amounting to R6 508 194. Therefore I was unable to confirm or verify by alternative means the existence and valuation of this balance.

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16. I was unable to obtain sufficient appropriate audit evidence for journals amounting to R97 417 576 posted against receivables for VAT. The existence, rights and obligations, and valuation of these journals could not be confirmed.

17. The bad debts written off amounting to R55 245 178 for the financial year were not disclosed in consumer debtors in note 10 to the financial statements. I was unable to confirm or verify the classification, understandability and compliance.

Payables

18. I was unable to obtain sufficient appropriate audit evidence for the suspense creditors accounts and provision of accruals included in creditors to the amount of R11 569 191. Therefore creditors to the amount of R11 569 191 could not be confirmed or verified for existence, valuation, and rights and obligations.

19. An amount of R17 246 989 being VAT on debtors not received was not included in creditors. Had this amount been correctly disclosed, creditors would have been reported as R37 807 403 and appropriated funds would have decreased by R17 246 989.

Statutory fund

20. With reference to accounting policy note 5.1, the municipality's accounting policy is to contribute annually a minimum of 7,5% of assessment rates of the immediately preceding year to the Consolidated Capital Development and Loans Funds. No contribution has been made for the financial year ended 30 June 2009. Had the contribution been made, statutory funds would have been stated at R191 173 002 in the balance sheet while contributions would have increased by R9 454 309. Furthermore, statutory funds amounting to R59 265 687 showed no movement and therefore I was unable to confirm the valuation and existence of these funds.

21. An amount of R5 131 140 included as other income in the statutory funds relates to the deposits for the sales of plots during the financial year. I was unable to obtain sufficient appropriate audit evidence regarding the details of these sales of plots. Creditors are understated by R5 131 140 while long-term debtors and profit on the sale of plots are understated and fixed assets overstated by an unknown amount.

Trust funds and reserve

22. Trust funds of R4 457 858 was in debit for the year. Had this been corrected, trust funds would increased with R4 457 858 while contributions would have increased with the same amount.

Accumulated surplus

23. I was unable to obtain sufficient appropriate audit evidence for journals amounting to R3 345 732 posted against accumulated surplus. The valuation, existence and rights, and obligation of these journals could not be confirmed or verified.



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Revenue

24. Grants and subsidy of R57 907 190 as conditional grant income, of which the conditions have been met, was incorrectly allocated to other service charges and not to grants and subsidies. Had this error not occurred, the grant and subsidies would have increased by R3 519 643 while other income would have decreased by the same amount.

25. I was unable to obtain sufficient appropriate audit evidence for an unexplained difference of R4 862 551 between the property rates per the financial statements and the ratable valuation reconciliations. Furthermore, no interim valuations were performed for properties that were effected by improvements. Therefore I was unable to confirm or verify by alternative means the completeness and accuracy of assessment rates to the value of R136 036 853 as stated in the income statement.

26. Incorrect tariffs used to levy refuse, water and sewage income resulted in other service revenue being understated by R3 690 614. Had this been correctly levied, debtors and revenue would have increased by R3 690 614.

Expenditure

27. I was unable to obtain sufficient appropriate audit evidence for journals amounting to R14 889 813 posted against expenditure. The accuracy, occurrence and classification of these journals could not be confirmed or verified.

Employee cost

28. I was unable to obtain sufficient appropriate audit evidence for an unexplained difference of R6 012 116 between the employee cost total in the financial statements and the payroll system reconciliation. Therefore I was unable to confirm or verify by alternative means the completeness and accuracy of employee cost to value of R130 761 192 as stated in the income statement.

Contingent liabilities

29. I was unable to obtain sufficient appropriate audit evidence for contingent liabilities to the amount of R12 700 000 disclosed in note 24 to the financial statements. I was therefore unable to confirm or verify through alternative means the existence, rights and obligations, valuation and completeness of contingent liabilities.

Commitments

30. The specimen IMFO statements require commitments to be disclosed as approved and they should not be approved with the inclusion of how commitments will be funded during the forthcoming financial year, being internal or external funds. I was unable to confirm or verify the amounts for such disclosure. Furthermore, I was unable to obtain sufficient appropriate audit evidence for contracts entered into by the municipality to the value of R17 100 000 that formed part of the commitment disclosure. Therefore I was unable to confirm or verify the existence, rights and obligations, and valuation of commitments to the value of R37 378 279 included in note 24 to the financial statements.



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Unauthorised expenditure

31. Operating expenditure exceeded the adjusted budget of R309 166 000 by R3 128 594. This is deemed as unauthorised expenditure in terms of section 32 of the MFMA and this amount has not been disclosed as unauthorised expenditure. This is contrary to section 125(2)(d) of the MFMA, which requires disclosure of irregular expenditure in the annual financial statements.

Disclaimer of opinion

32. Because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

Basis of accounting

33. The municipality's policy is to prepare financial statements on the entity-specific basis of accounting, as set out in accounting policy note 1.1.

Other matters

I draw attention to the following matters that relate to my responsibilities in the audit of the financial statements:

Other information included in the annual report

34. I have not obtained the other information included in the annual report and have not been able to identify any material inconsistencies with the financial statements.

Unaudited supplementary schedules

35. The supplementary information set out on pages 99 to 128 does not form part of the financial statements and is presented as additional information. I have not audited these appendices and accordingly do not express an opinion thereon.

Non-compliance with applicable legislation

Municipal Finance Management Act

36. Contrary to section 65(2)(e) of the MFMA invoices to the amount of R4 330 436 were not paid within the 30 days as required.

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Municipal Systems Act

37. Contrary to section 7(1) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA), councillors did not declare their interest in companies on an annual basis.

Governance framework

38. The governance principles that impact the auditor's opinion on the financial statements are related to the responsibilities and practices exercised by the accounting authority and executive management and are reflected in the internal control deficiencies and key governance responsibilities addressed below:

Internal control deficiencies

39. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes that gave rise to the deficiencies in the system of internal control, which led to the disclaimer of opinion. The root causes are categorised according to the five components of an effective system of internal control (the number listed per component can be followed with the legend below the table.)

Par. no.	Basis for disclaimer of opinion	CE	RA	CA	IC	M
4	Cash and bank	7	4	4	1	1
5	Investments	7	4	4	1	3
6 – 9	Property, plant and equipment	5	2	3	3	3
10 – 11	Long-term liabilities	7	4	4	1	1
12 – 17	Receivables	5	2	3	3	3
18 – 19	Payables	7	4	4	1	1
20 – 21	Statutory funds	5	2	3	3	3
22	Trust funds	5	2	3	1	3
23	Accumulated surplus	7	4	4	1	1
24 – 26	Revenue	5	2	3	3	3
27	Expenditure	7	4	4	1	1
28	Employee cost	5	2	3	1	3
29	Contingent liabilities	7	4	4	1	1
32	Commitments	7	4	4	1	1
31	Unauthorised expenditure	7	4	4	1	3

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40. The basis of qualification paragraphs could have been avoided had care been taken with regard to independent review and reconciliations of account balances as well as the safeguarding of information for audit purposes.

Legend

CE = Control environment

The organisational structure does not address areas of responsibility and lines of reporting to support effective control over financial reporting.	1
Management and staff are not assigned appropriate levels of authority and responsibility to facilitate control over financial reporting.	2
Human resource policies do not facilitate effective recruitment and training, disciplining and supervision of personnel.	3
Integrity and ethical values have not been developed and are not understood to set the standard for financial reporting.	4
The accounting officer/accounting authority does not exercise oversight responsibility over financial reporting and internal control.	5
Management's philosophy and operating style do not promote effective control over financial reporting.	6
The entity does not have individuals competent in financial reporting and related matters.	7

RA = Risk assessment

Management has not specified financial reporting objectives to enable the identification of risks to reliable financial reporting.	1
The entity does not identify risks to the achievement of financial reporting objectives.	2
The entity does not analyse the likelihood and impact of the risks identified.	3
The entity does not determine a risk strategy/action plan to manage identified risks.	4
The potential for material misstatement due to fraud is not considered.	5

CA = Control activities

There is inadequate segregation of duties to prevent fraudulent data and asset misappropriation.	1
General information technology controls have not been designed to maintain the integrity of the information system and the security of the data.	2
Manual or automated controls are not designed to ensure that the transactions have occurred, are authorised, and are completely and accurately processed.	3
Actions are not taken to address risks to the achievement of financial reporting objectives.	4
Control activities are not selected and developed to mitigate risks over financial reporting.	5
Policies and procedures related to financial reporting are not established and communicated.	6
Realistic targets are not set for financial performance measures, which are in turn not linked to an effective reward system.	7

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IC = Information and communication

Pertinent information is not identified and captured in a form and time frame to support financial reporting.	1
Information required to implement internal control is not available to personnel to enable internal control responsibilities.	2
Communications do not enable and support the understanding and execution of internal control processes and responsibilities by personnel.	3

M = Monitoring

Ongoing monitoring and supervision are not undertaken to enable an assessment of the effectiveness of internal control over financial reporting.	1
Neither reviews by internal audit or the audit committee nor self -assessments are evident.	2
Internal control deficiencies are not identified and communicated in a timely manner to allow for corrective action to be taken.	3

Key governance responsibilities

41. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of key governance responsibilities, which I have assessed as follows:

No.	Matter	Y	N
Clear trail of supporting documentation that is easily available and provided in a timely manner			
1.	No significant difficulties were experienced during the audit concerning delays or the availability of requested information.		N
Quality of financial statements and related management information			
2.	The financial statements were not subject to any material amendments resulting from the audit.	Y	
3.	The annual report was submitted for consideration prior to the tabling of the auditor's report.		N
Timeliness of financial statements and management information			
4.	The annual financial statements were submitted for auditing as per the legislated deadlines in section 126 of the MFMA.	Y	
Availability of key officials during audit			
5.	Key officials were available throughout the audit process.		N
Development and compliance with risk management, effective internal control and governance practices			
6.	Audit committee		
	· The municipality had an audit committee in operation throughout the financial year.	Y	
	· The audit committee operates in accordance with approved, written terms of reference.		N
	· The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA.		N

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7.	Internal audit · The municipality had an internal audit function in operation throughout the financial year.	Y	
	· The internal audit function operates in terms of an approved internal audit plan.		N
	· The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA.		N
8.	There are no significant deficiencies in the design and implementation of internal control in respect of financial and risk management.		N
9.	There are no significant deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations.		N
10.	The information systems were appropriate to facilitate the preparation of the financial statements.	Y	
11.	A risk assessment was conducted on a regular basis and a risk management strategy, which includes a fraud prevention plan, is documented and used as set out in section 62(1)(c)(i) of the MFMA.		N
12.	Delegations of responsibility are in place, as set out in section 79/106 of the MFMA.	Y	
Follow-up of audit findings			
13.	The prior year audit findings have been substantially addressed.		N
14.	SCOPA/Oversight resolutions have been substantially implemented.	Y	
Issues relating to the reporting of performance information			
15.	The information systems were appropriate to facilitate the preparation of a performance report that is accurate and complete.		N
16.	Adequate control processes and procedures are designed and implemented to ensure the accuracy and completeness of reported performance information.		N
17.	A strategic plan was prepared and approved for the financial year under review for purposes of monitoring the performance in relation to the budget and delivery by the Municipality against its mandate, predetermined objectives, outputs, indicators and targets section 68 of the MFMA.	Y	
18.	There is a functioning performance management system and performance bonuses are only paid after proper assessment and approval by those charged with governance.	Y	

42. Management does not have the necessary controls in place to prevent, detect and correct material errors during the compilation of financial statements. This is evident from the number of limitation of scope issues relating to journals, payment vouchers and external support. Furthermore, independent reconciliations are not performed to ensure the correctness on internal data and records throughout the financial year.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

Report on performance information

43. I have reviewed the performance information as set out on pages 12 to 47.

The accounting officer's responsibility for the performance information

44. In terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality, prepared by the municipality in terms of section 46 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000)



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The Auditor-General's responsibility

45. I conducted my engagement in accordance with section 13 of the PAA read with General Notice 616 of 2008, issued in Government Gazette No. 31057 of 15 May 2008 and section 45 of the MSA.

46. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.

47. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the findings reported below.

Findings on performance information

Non-compliance with regulatory requirements

No quarterly reporting on performance information provided

48. No quarterly reports on the progress in achieving measurable objectives and targets were provided by the Mafikeng Local Municipality to facilitate effective performance monitoring, evaluation and corrective action, as required by the MSA.

Usefulness and reliability of reported performance information

49. The following criteria were used to assess the usefulness and reliability of the information on the municipality's performance with respect to the objectives in its integrated development plan:

- **Consistency:** Has the municipality reported on its performance with regard to its objectives, indicators and targets in its approved integrated development plan?
- **Relevance:** Is the performance information as reflected in the indicators and targets clearly linked to the predetermined objectives and mandate. Is this specific and measurable, and is the time period or deadline for delivery specified?
- **Reliability:** Can the reported performance information be traced back to the source data or documentation and is the reported performance information accurate and complete in relation to the source data or documentation?

The following audit findings relate to the above criteria:

Inconsistently reported performance information

50. The development priorities/objectives, indicators and targets in the integrated development plan are not consistent with those in the annual performance report.

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Subprogramme	Number of objectives
Integrated service delivery addresses improved basic municipal services and customer satisfaction	28
To encourage good corporate governance, public participation and ward committee system	12

51. The reported performance information did not include complete and comprehensive coverage of planned performance indicators and targets as per the SDBIP, IDP and budget.

Objective	Number of objectives
Enhance communication flow within and outside the municipality	1
To ensure an effective, efficient and sustainable financial management system in line with legislation	5
To ensure the provision of basic municipal services through integrated service delivery to the satisfaction of the customer	7
To provide quality, professional and sustainable integrated testing, licence registration services in accordance with relevant legislation	2
To provide effective, efficient fire, rescue and disaster management services that meet the expectation of the community	1
To render cost-effective and efficient and professional traffic management, law enforcement	5

Reported performance information not relevant

52. The key performance indicators as reported in the annual report is considered not measurable in terms of being time bound/deadline driven.

Objective	Number of objectives
Integrated service delivery addresses improved basic municipal services and customer satisfaction	28
To encourage good corporate governance, public participation and ward committee system	12

APPRECIATION

53. The assistance rendered by the staff of the Mafikeng Local Municipality during the audit is sincerely appreciated.

Signed by: *Auditor-General*

at Rustenburg on 05 February 2010



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence

